



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202

REPORT
NO. 90-071

May 22, 1990

MEMORANDUM FOR ASSISTANT SECRETARY OF DEFENSE (PRODUCTION AND LOGISTICS)
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Report on the Audit of the Financial Accounting and Reporting of the William Langer Jewel Bearing Plant (Project No. 9SS-0049)

Introduction

This is our final report on the Audit of the Financial Accounting and Reporting of the William Langer Jewel Bearing Plant (the Plant) for your information and use. Comments on a draft of this report were considered in preparing the final report. The audit was requested by the Assistant Secretary of Defense (Production and Logistics) and was performed from June to September 1989 at the Plant, Rolla, North Dakota. During the period August 1, 1985, through June 4, 1989, the Plant's annual sales of jewel bearings averaged \$3.3 million, and its annual costs of dosimeter operations averaged \$661,000.

Objectives and Scope

The audit objectives were to evaluate the Plant's financial management and the accuracy of the Plant's financial reporting. Specifically, we determined whether financial records and reports were in accordance with generally accepted accounting principles and governing regulations and whether the costs incurred in the operation of the facility were allowable in accordance with the terms of contract no. GS-00-DS-(P)-03003 and the applicable procurement regulations. We also evaluated the adequacy of internal controls and followed up on the recommendations made by the Inspector General (IG), General Services Administration (GSA), in Audit Report No. A50608/D/8/X6195, "Audit of Cost Reimbursable Contract: Bulova Watch Company, Inc., Contract No. GS-00-DS-(P)-03003 for the Period August 1, 1983, through July 31, 1985," March 27, 1986.

The principal period covered by this audit was from August 1, 1985, to June 4, 1989. We examined the Plant's accounting records, which included the general ledger accounts for the 46-month period ended June 4, 1989. We also examined the balance sheet as of June 4, 1989, and the income statements for the 46-month period then ended. Further, we reviewed the

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contract and contractor billings and the Plant's internal manuals and regulations. The audit was conducted in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, Department of Defense, and included such tests of internal controls as were considered necessary. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatements. In performing this financial and compliance audit, we evaluated the Plant's internal accounting controls and its compliance with laws and regulations. Our evaluation and a material weakness addressing the lack of financial controls over inventories of mounted jewel bearings are discussed beginning at page 3. Except as noted in this report, applicable internal controls were in place, items that we tested were in compliance with applicable directives and regulations, and there was no indication that items that we did not test were not also in compliance.

Background

The Plant is a Government-owned facility operated under contract no. GS-00-DS-(P)-03003 by Bulova Watch Company, Inc., a subsidiary of Lowes Corporation, Flushing, New York. Since 1953, the Plant has produced jewel bearings and related items for the Defense National Stockpile, DoD contractors, and private industry. In November 1981, the GSA contracting officer modified the existing contract to support the Federal Emergency Management Agency's (FEMA) need for a pilot production run of an unspecified number of dosimeters (small, hand-held, radiation-measuring devices). Because the jewel bearing plant (Building #1) did not contain sufficient space in which to produce the dosimeters, the Plant leased 14,000 square feet of manufacturing space (Building #2) built to FEMA specifications, and installed the necessary equipment to manufacture dosimeters. FEMA continues to fund the dosimeter operation. The Plant accounts for dosimeter operations using cash basis accounting procedures. The Plant accounts for jewel bearing operations using accrual basis accounting procedures.

Various contractual agreements have been in effect since the Plant's inception: the latest is a cost-plus-fixed-fee contract that provides for an annual fee of \$99,000. The contractor uses a revolving fund to finance the Plant's operation. The fund was initially established with advances from the Government and is used to deposit advances and sales proceeds and to pay for costs and fees incurred in the manufacture of jewel bearings and related items.

Effective October 1988, functional responsibility for the Plant was transferred by the Office of Management and Budget from the GSA to the Secretary of Defense. Effective April 1989, DoD delegated the authority to operate the Plant to the Director of the Defense Logistics Agency.

Prior Audit Coverage and Followup

The Inspector General, General Services Administration, issued Audit Report No. A50608/D/8/X6195, "Audit of Cost Reimbursable Contract: Bulova Watch Company, Inc., Contract No. GS-00-DS-(P)-03003 for the Period August 1, 1983, Through July 31, 1985," on March 27, 1986. (The contract cited in the title is the continuing contract between Bulova Watch Company and the U.S. Government for the operation of the Plant.) The audit objective was to determine the accuracy and reliability of the Plant's records and the allowability of the costs incurred. The GSA auditors stated that the Plant's financial statements did not fairly present its financial position. The auditors made 16 recommendations to the contracting officer regarding accounting procedures and adjustments to financial records at the Plant. The contracting officer concurred with all the recommendations and directed the Plant to either implement them or to implement acceptable alternative actions. We followed up on these recommendations to determine whether they had been effectively implemented. The results of our followup are discussed on page 5 of this report.

Results of Audit

Auditor's Opinion on Financial Statements. We examined the Plant's balance sheet as of June 4, 1989, and the related income statement for the 46-month period then ended. (The financial statements and our notes on these statements are in Enclosure 1.) The Plant did not prepare a statement of changes in financial position for our review. Presentation of such a statement, which summarizes a company's financing and investing activities and other changes in financial position, is required by generally accepted accounting principles, but is not required under the terms of the contract.

The Plant's financial statements did not properly reflect an obligation under a capital lease or recognize interest expenses associated with each lease payment and did not account for rental income derived from the capital lease asset. (These matters are fully discussed in Enclosure 1, notes 10, 16, and 23.) As a result, during the 46-month period ended June 4, 1989, the net asset value of the capital lease was overstated by \$75,394, and the obligation under the capital lease was overstated by \$251,289. Further, the operating profit for both current and prior years' equity, was understated by \$211,288, which represented rental income for the 62-month period ended June 4, 1989. Rental income for the initial 16-month period, April 1984 through July 1985, was \$35,393, and rental income for the 46-month period, August 1985 through June 4, 1989, was \$175,895.

The operating supplies inventory of blanks, raw material for making jewel bearings, totaling \$235,983, may have been substantially overstated (Enclosure 1, note 5) because it

included items for which the Plant had no use in recent years, and the Plant did not have a policy for identifying and writing off obsolete operating supply inventories.

Pre-Operating Costs valued at \$1,745,151, and the equity they represent, were not properly accounted for. As discussed in Enclosure 1, notes 12 and 17, those costs did not represent assets or equity that were relevant to the financial position or operation of the Plant.

As discussed in Enclosure 1, notes 13 and 14, personnel at the Plant did not record the cost of all Operating and Administrative Equipment contained in Building #2 and did not account for depreciation of that equipment. Generally accepted accounting principles require the financial control of direct purchased and transferred equipment. Accordingly, the fixed asset and appropriated capital accounts were understated. The Plant did not have data available on the value of the equipment not accounted for; however, based on equipment listings, we believe it represents a material amount.

Contrary to generally accepted accounting principles, the Plant had not properly established financial control over mounted jewel bearing inventories. As discussed in Enclosure 1, note 3, proper accounting for these items would increase inventories and operating profits by about \$14,270.

As a result of the matters discussed above, the financial statements did not present fairly, in conformance with generally accepted accounting principles, the Plant's financial position as of June 4, 1989, or the results of its operations for the 46-month period then ended.

Report on Internal Accounting Controls and Compliance With Laws and Regulations. We have examined the Plant's financial statements for the 46 months ended June 4, 1989. As part of our audit, we evaluated the Plant's internal accounting controls to the extent we considered necessary to conform with generally accepted government auditing standards.

The purpose of our evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the Plant's financial statements. For purposes of this report, we classified the significant internal accounting controls as cash and receivables, inventories, fixed assets, payables and liabilities, fund balances, and payrolls. Our audit included all of these control categories.

The Plant's management is responsible for establishing and maintaining an effective system of internal accounting controls. To fulfill this responsibility, management must estimate and judge the expected benefits and related costs of control procedures. The objectives of a system of internal

accounting controls are to provide management with reasonable assurance that obligations and costs are in compliance with applicable laws; funds, property, and assets are safeguarded against waste, loss, and unauthorized use or misappropriation; and assets, liabilities, revenues, and expenditures applicable to operations are properly recorded and accounted for to permit the preparation of reliable financial statements and to maintain accountability over the Plant's assets. Because of inherent limitations in any system of internal accounting controls, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with procedures may deteriorate.

Our evaluation, which was made for the limited purpose described in the second paragraph of page 1, would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the Plant's system of internal accounting controls taken as a whole. However, our audit showed that there were no financial controls over inventories of mounted jewel bearings (see Enclosure 1, note 3). Without such controls, management had no assurance that sales of usable mounted jewel bearings were being properly recorded and reported.

As part of our audit, we also tested the Plant's compliance with the provisions of the contract with the Bulova Watch Company, Inc. -- reimbursable contract no. GS-00-DS-(P)-03003. In our opinion, the Plant generally complied with the provisions of the contract for transactions tested that could have materially affected its financial position. In making our audit, nothing came to our attention that caused us to believe that the Plant was not complying with the provisions of the contract for those transactions not tested.

Results of Followup on GSA Report. Our followup of the previous GSA IG audit report showed that nine recommendations were effectively implemented, three recommendations were partially implemented, and four recommendations were not implemented. The status of conditions relating to recommendations that were either partially implemented or were not implemented at the time of our audit follows.

Recommendations Partially Implemented. The GSA IG recommended establishing a cost pool to prorate General and Administrative expenses between the jewel bearing and dosimeter operations. The Plant had established a cost pool; however, it did not provide for a reasonable allocation of expenses to the dosimeter operations (see page 8). The GSA IG also recommended adjusting entries to establish proper accounting for Building #2, a leased asset, and its related obligation and to disclose the expenses associated with the rental of the building. We found

that the entries were incomplete (Enclosure 1, note 17). In addition, the GSA IG recommended making a separate inventory of administrative and plant production equipment that FEMA furnished at no cost to the contractor and establishing memorandum accounts so that the inventory could be reconciled against the account balances. The Plant inventoried the equipment; however, the Plant did not obtain the cost basis of the equipment from FEMA. Therefore, the financial records or reports did not reflect the equipment value, and reconciliations had not been performed (Enclosure 1, notes 13 and 14).

Recommendations Not Implemented. The GSA IG recommended that the Plant return cash balances in excess of \$365,000 to GSA. Effective cash management practices had not been established, which resulted in the plant maintaining excessive cash balances. Cash management at the Plant is discussed on page 7 of this report. In addition, the GSA IG recommended establishing an inventory account for mounted jewel bearings. The Plant did not establish this account (Enclosure 1, note 3). Further, the GSA IG recommended that the Plant depreciate leasehold improvements and operating and administrative equipment associated with dosimeter operations. The Plant did not depreciate those items (Enclosure 1, notes 11, 13, and 14). Finally, related to dosimeter operations, the GSA IG recommended that the Plant cease charging dosimeter operating expenses to the Pre-Operating Cost asset account; that operating costs charged to the Pre-Operating Cost asset account after October 1, 1983, be expensed; and that the balance in the Pre-Operating Cost asset account on September 30, 1983, be amortized against the dosimeter operations. The Plant did not stop charging operating costs to the Pre-Operating Cost account until October 1, 1986, and, as of the time of the audit, had not amortized any of those costs (Enclosure 1, note 12).

Allowability of Costs. The costs that the Plant incurred were generally in compliance with contract terms and the applicable procurement regulations, with one exception. The Plant reimbursed employees for the cost of eye examinations and safety glasses under its written policy, which states, "The Plant pays the cost of safety equipment for those employees whose working conditions without same, in the opinion of the General Manager, are potentially hazardous to the employee." In our opinion, this policy was not intended to cover the cost of treating extraordinary eye conditions, such as the cataract problems experienced by the Plant's General Manager. During the 46 months (3.83 years) covered by our audit, we identified 81 employees who requested reimbursement for amounts above \$50 for eye examinations and safety glasses. The total reimbursement made to employees was \$12,703, or an average of \$39 per employee per year. During the same period, similar costs for the General Manager amounted to \$1,235, or an average of \$322 per year. We believe that the \$283 difference in average costs between the employees and the General Manager (\$39 versus \$322) was not

reasonable or necessary to effect an adequate measure of safety protection and should not have been reimbursed by the Government. Accordingly, the excessive costs of \$1,084 (3.83 years x \$322 per year) should be disallowed.

Other Matters of Interest

Cash Management. Cash maintained in local bank accounts routinely exceeded the amount needed for day-to-day Plant operation. This occurred because the Plant based average cash needs on gross monthly disbursements instead of managing cash to meet actual payment due dates. Any reductions in outstanding cash would result in decreases in interest payments that the U.S. Treasury must make.

As shown below, the average monthly cash balance that the Plant maintained for the 46 months ended June 4, 1989, exceeded FY 1989 average monthly operational expenses by over \$100,000.

Cash Comparison

<u>Average Monthly</u>	Jewel Bearing Operations	FEMA Dosimeter Operations	Total
Cash Balance-Actual	\$365,997	\$77,110	\$443,107
Operating Costs-Accrued (Excludes Depreciation)	<u>278,804</u>	<u>64,107</u>	<u>342,911</u>
Monthly Cash Excess	<u>\$ 87,193</u>	<u>\$13,003</u>	<u>\$100,196</u>

Payroll costs and related benefits make up about 81 percent of operating costs with the weekly payroll of less than \$50,000 being the Plant's major disbursing concern. The Plant manager stated that due to past delays in replenishing cash, a large balance was necessary to ensure that adequate cash was on hand to meet disbursing needs. Receipts for sales of jewel bearings averaged \$257,000 per month. While FEMA did occasionally delay advancing cash to the Plant, cash balances at the Plant rarely fell below \$100,000.

The nature of the Plant's disbursements offers significant opportunities for reducing cash levels. We did not perform a detailed analysis of cash needs, but, in our opinion, no more than 2 weeks' average operating costs, or about \$172,000 based on FY 1989 costs, should be allowed to accumulate in local accounts.

f. Establish and maintain adequate financial controls over spare parts inventory (Enclosure 1, note 6).

g. Establish and maintain adequate financial control over special tooling (Enclosure 1, note 7).

h. Establish and maintain adequate financial controls over Other--FEMA items (Enclosure 1, note 8).

i. Record the cost of in-house construction for Building #1 and account for depreciation of the building addition (Enclosure 1, note 9).

j. Account for depreciation of the Leased Land-Building, Capital Lease--Building #2 (Enclosure 1, note 10).

k. Account for depreciation of Leasehold Improvements--Building #2 (Enclosure 1, note 11).

l. Write off the Pre-Operating Cost--Building #2 and related equity (Enclosure 1, note 12).

m. Establish financial controls over all Building #2 operating equipment, both purchased and transferred, and account for depreciation of all of this equipment (Enclosure 1, note 13).

n. Establish financial control over all Building #2 administrative equipment and account for depreciation of this equipment (Enclosure 1, note 14).

o. Adjust the balance of Obligations Under Capital Lease and properly account for monthly lease payments (Enclosure 1, note 16).

p. Adjust the Appropriated Capital--FEMA account to correct the accounting errors and write off the Pre-Operating Cost (Enclosure 1, note 17).

q. Adjust the operating profit for prior and current years to recognize income and expenses derived from the rental of Building #2 (Enclosure 1, notes 18 and 19).

r. Prepare and submit a statement of changes in financial position in its periodic financial report submissions.

s. Provide for a reasonable allocation of General and Administrative Expenses to jewel bearing and dosimeter operations (page 8).

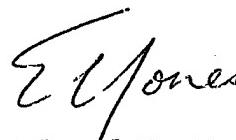
2. We recommend that the Defense Logistics Agency contracting officer disallow \$1,084 as unreasonable costs relating to optical safety (page 6).

On December 26, 1989, we provided a copy of the draft report to the Assistant Secretary of Defense (Production and Logistics) and the Director, Defense Logistics Agency. We received reply to the draft report from the Director, Defense Logistics Agency, through the Assistant Secretary of Defense (Production and Logistics) on April 30, 1990. The complete text of management's comments is provided in Enclosure 2. Management concurred with the findings and recommendations, and actions taken or planned should correct the conditions disclosed. Management comments to the draft report comply with the provisions of DoD Directive 7650.3, and a response to this final report is not required.

No monetary benefits are claimed in this report. Internal controls were inadequate and account balances were inaccurate, as discussed throughout the report. Recommendations in this report address internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Therefore, a copy of the final report will be provided to the senior official responsible for internal controls within the Defense Logistics Agency.

The cooperation and courtesies extended to the audit staff during the audit are appreciated. If you have any questions concerning this report, please contact Mr. James Helfrich at (614) 238-4141 (AUTOVON 850-4141) or Mr. John Gregor at (202) 693-0633 (AUTOVON 223-0633). A list of the Audit Team Members is in Enclosure 3.

Copies of this report are being distributed to the activities shown in Enclosure 4.


Edward R. Jones
Deputy Assistant Inspector General
for Auditing

Enclosures

WILLIAM LANGER JEWEL BEARING PLANT
STATEMENT OF FINANCIAL CONDITION
As of May 31, 1989 ^{1/}

ASSETS

Current

Cash In Bank: (note 1) ^{2/}			
FEMA	\$ 89,801		
DLA-N	<u>321,115</u>		
BC/DLA-N Special Account	<u>410,916</u>		
Payroll Account	<u>500</u>		\$ 411,416

Accounts Receivable:

Trade Bldg. #1 (note 2)	253,412		
Stockpile Bldg. #1	<u>525,009</u>		\$ 778,421

Inventories: (note 3)

Finished Goods On Hand (note 4)	788,814		
Work-In-Process	<u>518,812</u>		

Operating Supplies:

Blanks (note 5)	\$235,983		
Diamond Powder	16,238		
Stock Room	72,412		
Spare Parts (note 6)	88,698		
Special Tooling (note 7)	9,005		
Other-FEMA (note 8)	<u>949</u>		\$1,730,911
	<u>423,285</u>		

Deferred Charges & Prepaid Expenses Bldg. #1	<u>28,627</u>		
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TOTAL CURRENT ASSETS			\$2,949,375
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FIXED ASSETS

	Cost Basis	Accumulated Depreciation	Net Value
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Land Bldg. #1	\$ 18,438		\$ 18,438
Building & Land Improve. Bldg.-#1 (note 9)	1,524,393	\$ 265,370	<u>1,259,023</u>
Leased Land-Bldg. Cap. Lease Bldg.-#2 (note 10)	788,566	26,224	762,342
Leasehold Improvements- Bldg. #2 (note 11)	408,811		408,811
Pre-Operating Cost- Bldg. #2 (note 12)	1,745,151		1,745,151
Operating Equipment- Bldg. #1	1,188,161	921,891	266,270
Operating Equipment- (note 13) Bldg. #2	224,399		224,399
Administrative Equip.- Bldg. #1	92,065	40,863	51,202
Administrative Equip.- Bldg. #2 (note 14)	23,332		23,332
Total	<u>\$6,013,316</u>	<u>\$1,254,348</u>	

TOTAL FIXED ASSETS			\$4,758,968
TOTAL ASSETS			<u>\$7,708,343</u>

^{1/} Actually as of June 4, 1989, not as of May 31, 1989, as reported.

^{2/} Notes begin on page 4 of this enclosure.

WILLIAM LANGER JEWEL BEARING PLANT
STATEMENT OF FINANCIAL CONDITION
As of May 31, 1989 (continued)

LIABILITIES

Accounts Payable:

Trade	\$ 92,823
Rolla Development Corporation (FEMA Rent)	12,246
Federal Unemployment Insurance	(1,136)
State Unemployment Insurance	5,194
Pension (note 15)	<u>335,927</u>
	<u>\$ 445,054</u>

Leave Liability:

Holiday	\$ 2,410
Vacation	71,956
Christmas Bonus	9,000
Accrued Payroll	32,433
Deductions Savings Bonds	2,560
Federal Withholding Taxes Payable	11,920
State Taxes Withheld	8,570
Life Insurance Deductions	2,434
Deferred Credits (FEMA)	<u>89,801</u>
	<u>\$ 231,084</u>

TOTAL CURRENT LIABILITIES \$ 676,138

OBLIGATION UNDER CAPITAL LEASE-BLDG. #2 (note 16) 726,949

INVESTMENT OF U.S. GOVERNMENT

Invested Cap./Tech. Improvements	\$ 615,033
Prov. for Tech. Improvements of Equipment	588,592
Appropriated Capital: DLA-N	2,578,792
Appropriated Capital: FEMA (note 17)	2,425,789
Operating Profit or (Loss) - Prior Years (note 18)	31,609
Operating Profit or (Loss) - Current Year (note 19) ^{3/}	70,559
Resources Reserved for Fuel Storage Repair	<u>(5,118)</u>

TOTAL INVESTMENT OF U.S. GOVERNMENT \$6,305,256

TOTAL LIABILITIES AND INVESTMENT OF U.S. GOVERNMENT \$7,708,343

^{3/} Also see notes 2, 3, 4, and 5.

WILLIAM LANGER JEWEL BEARING PLANT
STATEMENT OF INCOME
FOR THE PERIOD AUGUST 1, 1985, THROUGH JUNE 4, 1989

Sales

Jewel Bearings	\$12,112,994
Mounting Service (note 20)	<u>419,791</u>
 TOTAL SALES	 \$12,532,785

Cost of Goods Sold

Materials (Blanks)	\$ 231,085
Direct Labor	5,396,433
Other	6,641,981
Mounting Service Cost (note 21)	<u>371,173</u>
	\$12,640,672

Add: Beginning Inventories:

Finished Goods	\$ 621,793
Work-In-Process	<u>582,156</u>
	1,203,949

Less: Inventory Transfers In/Out - Net (note 22) 122,492

Less: Ending Inventories:

Finished Goods	\$ 798,899
Work-In-Process	<u>518,812</u>
	1,317,711

TOTAL COST OF GOODS SOLD \$12,404,418

Operating Income	128,367
Other Income (note 23)	179,185
Other Expenses (note 24)	<u>(155,699)</u>

Net Income: \$ 151,853

Prior Period Adjustments (note 25)	(29,500)
Net Income For Period (notes 2, 3, 4, and 5)	<u>\$ 122,353</u>

WILLIAM LANGER JEWEL BEARING PLANT
NOTES TO FINANCIAL STATEMENTS

Note 1. Cash In Bank. The account balance of \$411,416 was correct, but, based on operating requirements, we considered that the amount of cash that was kept in the William Langer Jewel Bearing Plant (the Plant) bank account was excessive. See discussion on page 7 of the report.

Note 2. Accounts Receivable, Trade. The balance of \$253,412 was overstated by \$727, which represented the value of two delinquent customer accounts that should have been written off in accordance with Article VIII of the contract. The overstatement represented a corresponding overstatement of operating profit and net income.

Note 3. Inventories. Inventories were understated by about \$14,270 because the Plant had not established an inventory account for on-hand, potentially salable stocks of mounted jewel bearings. To allow for defects or spoilage of jewel bearings in the mounting process, the Plant customarily sent the mounting contractor a larger number of unmounted jewel bearings than the number of mounted bearings required to satisfy a customer order. The value of these extra unmounted jewel bearings was written off of the Finished Goods Inventory and reported under Mounting Service Cost when the bearings were shipped to the mounting contractor. The number of mounted jewel bearings that was returned from the mounting contractor was generally larger than the number needed to fill the customer order. The Plant retained the extra, mounted jewel bearings and maintained informal records as to the number on hand. However, the value of this inventory was not formally accounted for on the balance sheet. Thus, there was no financial control over the on-hand stock of mounted jewel bearings. The understatement of inventory represented a corresponding understatement of operating profit and net income.

Note 4. Finished Goods On Hand. The balance of \$788,814 was overstated by \$26,151 because it included the value of inactive items. The Plant requested approval to write off the inactive items in October 1988 and was still awaiting approval from the contracting officer at the time of our audit. The overstatement of finished goods represented a corresponding overstatement of operating profit and net income.

Note 5. Blanks. The reported balance of \$235,983 is correct, but the actual value of usable blanks (raw material) for manufacturing jewel bearings may have been lower because of obsolescence. The Plant had no procedure for reviewing and writing off obsolete blanks in inventory. Our review of 23 items, valued at \$84,324, in this inventory indicated that 9 items, valued at \$24,981, had not been used since before 1984.

WILLIAM LANGER JEWEL BEARING PLANT
NOTES TO FINANCIAL STATEMENTS (continued)

Note 6. Spare Parts. The spare parts inventory included items for which there was no recorded or reported value and items that were produced at the Plant and entered into inventory at catalog prices rather than at the cost of production. We could not determine the value of unpriced or catalog-priced items.

Note 7. Special Tooling. The balance of \$9,005 could not be verified. Records that identified quantitative balances and costs of individual items were not maintained, and physical inventories could not be conducted to verify the account balance.

Note 8. Other -- FEMA. The balance of \$949 could not be verified. Records that identified quantitative balances and costs of individual items were not maintained, and physical inventories could not be conducted to verify the account balance.

Note 9. Building and Land Improvements -- Building #1. The reported balance was understated by about \$20,600 because of unrecorded in-house construction and was overstated by about \$13,700 because of unrecorded depreciation, a net understatement of about \$6,900. This understatement represented a corresponding understatement of operating profit and net income.

a. The balance did not include labor and indirect costs associated with in-house construction of capital assets by Plant personnel. Records indicated that 1,373 hours of direct labor valued at about \$14,600, exclusive of associated indirect costs, were incurred on in-house construction between April 1988 and May 1989. We did not identify all associated indirect costs, but we estimated that fringe benefits alone would have totaled about \$6,000.

b. The balance improperly excluded the cost of depreciation for FY 1989 for the new building additions that were occupied beginning April 1988. Based on the value of the property recorded as of September 30, 1988, we estimated that the depreciation for the 8 months ended May 1989 was \$13,704.

Note 10. Leased Land-Building, Capital Lease -- Building #2. The balance of \$762,342 was overstated by \$75,394. The reported accumulated depreciation of \$26,224 was only through July 1985. The unreported depreciation expense for the period August 1985 through May 1989 was \$75,394 (46 months x \$1,639 per month). Also, see notes 18 and 19.

WILLIAM LANGER JEWEL BEARING PLANT
NOTES TO FINANCIAL STATEMENTS (continued)

Note 11. Leasehold Improvements -- Building #2. The account balance of \$408,811 did not reflect any depreciation of leasehold improvements. The Plant treated those assets as though they belonged to the Federal Emergency Management Agency (FEMA) because FEMA had reimbursed the Plant for the purchase of those assets. We could not determine the amount of depreciation that should have been accumulated as of June 4, 1989. Based on Plant records, over \$300,000 of these improvements was made in 1983, and depreciation should have commenced thereafter.

Note 12. Pre-Operating Costs -- Building #2. The Pre-Operating Costs valued at \$1,745,151 and the corresponding equity (Appropriated Capital: FEMA) were not properly accounted for. The costs represent intangibles such as labor, utilities, and rental expenses that were accumulated through October 1, 1986, in anticipation of a mass production of dosimeters, at which time the balance would be amortized against such production. However, in a Statement of Work dated March 31, 1984, FEMA documented that, based on congressional testimony, the Plant would not be used for mass production. This Statement of Work provision was still in effect as of the time of our audit.

These costs were entirely financed by, and reported to, FEMA. Without mass production of dosimeters by the Plant, there is no substantive basis for amortizing such costs and, in our opinion, no useful purpose is served in continuing to report these costs as Plant assets. Accordingly, the full Pre-Operating Cost fixed asset balance and the associated Appropriated Capital: FEMA (see Note 17) amount should be written off of the Plant's records.

Note 13. Operating Equipment -- Building #2. The balance of \$224,399 could not be verified. We identified understatements and overstatements, but could not determine the net amount misstated in this account.

a. The Operating Equipment -- Building #2 represents equipment that the Plant purchased for FEMA's dosimeter operations. The balance of \$224,399 did not reflect the value of all of the operating equipment associated with the dosimeter operation. For example, the balance did not include equipment provided by FEMA at no cost to the Plant. The Plant accounted for the operating equipment provided by FEMA on an item basis, but not on a financial basis. Records were not available at the Plant for us to determine the value of the operating equipment that the Plant did not purchase.

b. The balance of \$224,399 also did not reflect any depreciation expense. FEMA reimbursed the Plant for the purchase

WILLIAM LANGER JEWEL BEARING PLANT
NOTES TO FINANCIAL STATEMENTS (continued)

price of this operating equipment. We could not readily determine the amount of depreciation that the Plant should have accumulated as of June 4, 1989. Plant records indicated that most of the equipment represented by this account was purchased before 1985.

Note 14. Administrative Equipment -- Building #2. We could not verify the balance of \$23,332, which represented the acquisition value of administrative equipment that the Plant purchased for the FEMA dosimeter operation. However, the account did not include the value of administrative equipment that was provided by Government activities for the dosimeter operation, and we could not determine the value from records at the Plant. Thus, we could not readily determine the amount of depreciation that should have been reported. Moreover, our review indicated that most of the administrative equipment was acquired before 1986, and depreciation should have commenced thereafter.

Note 15. Pension. Our verification of this account balance was limited to billings and other documentation that Bulova Watch Company, Inc., provided to the Plant.

Note 16. Obligations Under Capital Lease -- Building #2. The balance of \$726,949 was overstated by \$251,289, which represented the principal portion of the lease payments for the period August 1, 1985, through June 4, 1989. The Plant did not properly account for the paid principal on the lease as a reduction to its obligation under the capital lease. Also, the Plant did not make the general disclosure required under generally accepted accounting principles as to lease terms, renewals, and payments. Under provisions of a lease dated April 1, 1984, the Plant, as the Government's agent, is obligated to pay an annual rental of \$146,952 at the rate of \$12,246 per month to the Rolla Development Corporation (the lessor) through September 1, 1993. Upon completion of the initial lease period, the Government may renew for two additional 10-year periods at a rental of \$4,000 per year plus an additional rental reimbursement for local real property taxes that are assessed on the premises, or the Government can purchase the premises for the sum of \$1.00 and pay any and all closing costs associated with the transfer of the title. Information on minimum future lease payments follows.

WILLIAM LANGER JEWEL BEARING PLANT
NOTES TO FINANCIAL STATEMENTS (continued)

<u>Fiscal Year Ended</u>	<u>Amount</u>
<u>September 30</u>	
Minimum Future Lease Payments:	
1989 (6/1/89 thru 9/30/89)	\$ 48,984
1990	146,952
1991	146,952
1992	146,952
1993 (10/1/92 thru 8/31/93)	134,706
Total Minimum Lease Payments	<u>\$624,546</u>
Less: Imputed Interest*	<u>148,937</u>
Present Value of Net Minimum Lease Payments	<u>\$475,609</u>

*Based on an imputed interest rate of 13.245 percent that was derived from a total asset value of \$788,566 and monthly payment of \$12,246 for 113 months.

Note 17. Appropriated Capital -- FEMA. The balance of \$2,425,789 was overstated by a net amount of \$1,768,298. As a result of the prior General Services Administration's audit, an adjustment of \$183,690 was made to the Pre-Operating Cost, which should have, but did not, result in a corresponding decrease in the FEMA capital account. Conversely, this account was improperly decreased by \$160,543 when interest and depreciation expenses relating to the capital lease for Building #2 were charged to this account instead of offset against the rental income for the property that it received from FEMA and reflecting the difference as other income.

Finally, the account was overstated by \$1,745,151 due to Pre-Operating Costs that should have been, but were not, written off of the Plant's records (see note 12).

Note 18. Operating Profit or Loss -- Prior Years. The balance of \$31,609 was understated by \$171,113 because rental income and expenses related to Building #2 were not properly accounted for from April 1984 through September 1988. Of the \$171,113 understatement, \$35,393 was attributable to the 16-month period before our audit.

Note 19. Operating Profit or Loss -- Current Year. The balance of \$70,559 was understated by \$40,175 because rental income and expenses relating to Building #2 were not properly accounted for from October 1988 through May 1989.

WILLIAM LANGER JEWEL BEARING PLANT
NOTES TO FINANCIAL STATEMENTS (continued)

Note 20. Mounting Service. The account represents the proceeds from sales of mounts only. Proceeds related to the jewel bearings housed in the mounts are reflected as jewel bearing sales.

Note 21. Mounting Service Cost. The account represents the cost of excess jewel bearings for mounting and the cost of mounting services performed. These costs were accounted for on a cash basis because the Plant did not maintain a separate mounted jewel bearing inventory account.

Note 22. The \$122,492 represents the net cost of goods sold inventory reductions reflected in the Plant's accounting records for the 46-month period ended June 4, 1989. Of the \$122,492, routine transfers involving Finished Goods Inventories (FGI) and Work-in-Process Inventories amounted to a \$47,077 net reduction. The Plant's periodic income statements provide for adequate disclosure of these transfers.

The remaining \$75,415, a FGI reduction, is attributable to the manner in which the Plant accounted for mounted jewel bearing services. Jewel bearings that were in excess of customer needs (see note 3) were included in FGI on the income statement, but not on the balance sheet. This practice was necessary because the Plant did not have a mounted jewel bearing inventory account. The \$75,415 was reflected in the income statement under Mounting Service Cost (see note 21).

Note 23. Other Income. The balance of \$179,185 was understated by \$179,696, which consisted of unrecognized income of \$175,895 related to the rental of the capital lease asset and \$3,801 related to the difference between actual and billed cost for services provided to FEMA from October 1986 through March 1987. The \$3,801 was properly reflected in the balance sheet, but was not shown on the income statement due to an oversight.

Note 24. Other Expenses. The \$155,699 represented pension expenses of \$98,000 incurred during FY 1986 that were not distributed to cost of goods sold and net inventory reductions of \$57,699 for the 46-month period.

Note 25. Prior Period Adjustments. The \$29,500 represented the net amount of adjustments related to prior expenses that the Plant made against the Operating Profit or Loss -- Prior Years' balance sheet account. We included these adjustments because they were made during the 46-month period included in our audit and because they affected total income for the period.



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100



16 MAR 1990

IN REPLY
REFER TO DLA-CI

MEMORANDUM THRU ASSISTANT SECRETARY OF DEFENSE (PRODUCTION AND
LOGISTICS) *by Bertram 4/27/90*

FOR DEPUTY ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DEPARTMENT OF DEFENSE

SUBJECT: Draft Report on the Audit of the William Langer Jewel
Bearing Plant (Project No. 9SS-0049)

Enclosed are our comments to the draft report in response to the
IG memorandum dated 26 December 1989.

FOR THE DIRECTOR:

20 Encls

Reatha E. Holmes
REATHA E. HOLMES
Chief, Internal Review Division
Office of Comptroller

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.a.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to initiate a cash management program to minimize the amount of cash maintained in its bank account. Follow cash management guidance contained in Chapter 32 of the DoD Accounting Manual 7220.9-M. ('Enclosure 1, note 1').

DLA COMMENTS: Concur with recommendation 1.a. A review of the plant's cash operating requirements will be made in accordance with DoD Accounting Manual 7220.9-M, Chapter 32, and the appropriate cash balance level established.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 Jun 90
() Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connolly

ENCLOSURE 2

Page 2 of 21

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.b.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to write off delinquent accounts receivable. (Enclosure 1, note 2).

DLA COMMENTS: Concur with recommendation 1.b. Procedures of DLAM 7000.1, chapter 11, govern the followup and write off of accounts receivable within DLA. When the plant cannot make collection on accounts receivable, they are reported to HQ DNSC for further action. At that time an allowance for uncollectibility is established. When followup does not obtain collection, then in accordance with DLAM 7000.1, chapter 11, write off of uncollectible accounts under \$100 can be authorized by the DNSC while uncollectible accounts over \$100 are forwarded to HQ DLA for appropriate disposition. This is the procedure that will be followed for the \$727.00 of old receivables mentioned in the audit report and any other accounts receivable where followup is considered necessary.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connnelly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049

RECOMMENDATION NUMBER 1.c.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish a financial inventory account for mounted jewel bearings. (Enclosure 1, note 3).

DLA COMMENTS: Concur with recommendation 1.c. Facts, as cited in the audit report regarding production and sale of mounted jewel bearings, indicate that proper accounting requires that they be recorded and presented in financial statements as an inventory asset. DLA will review production and accounting for mounted jewel bearings and provide instructions for establishing the inventory account.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL. Helen T. McCoy for Richard J. Connolly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.d.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to write off the value of inactive items in the finished goods inventory. (Enclosure 1, note 4).

DLA COMMENTS: Concur with recommendation 1.d. Written procedures are in effect governing the review and disposition of inactive items in the finished goods inventory. The contracting officer has acted on the Plant's request and has advised the Plant accordingly.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- Action is ongoing; Final Estimated Completion Date:
 Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connolly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.e.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish a procedure for identifying and writing off obsolete blanks (Enclosure 1, note 5).

DLA COMMENTS. Concur with recommendation 1.e. Procedures are in effect for the plant to request approval of the DLA contracting officer for extraordinary or unusual inventory adjustments. DLA will review the jewel bearing blank inventory and provide any needed additional instructions and procedures to the plant.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL. Helen T. McCoy for Richard J. Connolly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.f.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish and maintain adequate financial controls over spare parts inventory. (Enclosure 1, note 6).

DLA COMMENTS: Concur with recommendation 1.f. DLA will review the valuation and accounting practices for this inventory and provide the additional and appropriate instructions and procedures to the plant to assure the required financial control.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connally

TYPE OF REPORT: AUDIT

DATE OF POSITION: 22 Feb 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.g.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish and maintain adequate financial controls over special tooling. (Enclosure 1, note 7).

DLA COMMENTS: Concur with recommendation 1.g. DLA will review the operating and accounting procedures for special tooling inventory and costs and provide necessary and appropriate instructions and procedures to the plant.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connely

ENCLOSURE 2

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TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049

RECOMMENDATION NUMBER 1.h.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish and maintain adequate financial controls over other FEMA items. (Enclosure 1, note 8).

DLA COMMENTS: Concur with recommendation 1.h. This minor balance sheet inventory amount will be written off to expense. Small items of the kind it originally represented are currently expensed.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connally

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.i.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to record the cost of in-house construction for Building #1 and account for depreciation of the building addition. (Enclosure 1, note 9).

DLA COMMENTS: Concur with recommendation 1.i. We agree that generally accepted accounting practice requires that work performed by plant staff that adds to and enhances the value of a physical asset be capitalized at its cost value. The estimated amount of \$20,000 is small in relation to the total asset value, and depreciation on this amount would not have a material effect on statements of future operations and income. We are accepting the charging of these costs to operations and expense as they were incurred at the plant.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

ENCLOSURE 2

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TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.j.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to account for depreciation of the Leased Land-Building, Capital Lease, Building #2. (Enclosure 1, note 10).

DLA COMMENTS: Concur with recommendation 1.j. DLA will review the lease and other factors relevant to the value of the leased building and make appropriate estimate of its proper valuation. An amortization schedule will be provided to the plant, and annual charges will be made to a valuation allowance account and capital.

Nonconcur that an internal weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.k.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to account for depreciation of the Leasehold Improvements, Building #2. (Enclosure 1, note 11).

DLA COMMENTS: Concur with recommendation 1.k. DLA will review the all factors relevant to the value of the leasehold improvements and make appropriate estimate of their proper valuation. An amortization schedule will be provided the plant, and annual charges will be made to a valuation allowance account and capital.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

ENCLOSURE 2

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TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049

RECOMMENDATION NUMBER 1.1.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to write off the Pre-Operating cost - Building #2 and related equity. (Enclosure 1, note 12).

DLA COMMENTS: Concur with recommendation 1.1. These costs will be written off to reflect the fact that originally contemplated production is no longer likely.

Nonconcur that an internal control weakness exists for the weakness cited above.

DISPOSITION:

- (x) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connolly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.m.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish financial controls over all Building #2 operating equipment, both purchased and transferred, and account for depreciation of all of this equipment. (Enclosure 1, note 13).

DLA COMMENTS: Concur with recommendation 1.m. The DLA/DNSC staff will review the accounting basis for these assets. When reliable information is available values will be recorded for individual assets. Amortization adjustments will be recorded to capital to reflect current value of the asset account. The appropriate note will be included in the annual financial statements regarding assets not carried at their cost basis.

Nonconcur that an internal weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 Jun 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

ENCLOSURE 2

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TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.n.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to establish financial control over all Building #2 administrative equipment and account for depreciation of this equipment. (Enclosure 1, note 14)

DLA COMMENTS: Concur with recommendation 1.n. The DLA/DNSC staff will review the accounting basis for these assets. When reliable information is available, values will be recorded for individual assets. Amortization adjustments will be recorded to capital to reflect current value of the asset account. The appropriate note will be included in the annual financial statements regarding assets not carried at their cost basis.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connolly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 22 Feb 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.o.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to adjust the balance of obligation under capital lease and properly account for monthly lease payments. (Enclosure 1, Note 16)

DLA COMMENTS: Concur with recommendation 1.o. The DLA/DNSC staff will provide the lease amortization schedule to the plant and instructions for write down and subsequent monthly adjustments.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connally

ENCLOSURE 2

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TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.p.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to adjust the Appropriated Capital - FEMA account to correct the accounting errors and write off the Pre-Operating Cost. (Enclosure 1, note 17)

DLA COMMENTS: Concur with recommendation 1.p. The DLA will review this and related accounts and make adjustment of the Appropriated Capital-FEMA account including the write off of pre-operating costs, and asset and lease liability amortization.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 Jun 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049

RECOMMENDATION NUMBER 1.q.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to adjust the operating profit for prior and current years to recognize income and expenses derived from the rental of Building #2. (Enclosure 1, notes 18 and 19)

DLA COMMENTS: Concur with recommendation 1.q. The difference between the lease liability amortization and leased building amortization will be reflected in adjustments to the capital accounts. An appropriate note regarding disclosure of direct charges to the capital account will be included in annual financial statements.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 Jun 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049)

RECOMMENDATION NUMBER 1.r.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to prepare and submit a statement of changes in financial position in items periodic financial report submissions.

DLA COMMENTS: Concur with recommendation 1.r. This statement will be included in the annual financial statements of the Plant. DLA will provide appropriate instructions.

Nonconcur that an internal control weakness exists for the reasons cited above.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 Jun 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

TYPE OF REPORT: AUDIT

DATE OF POSITION: 16 Mar 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049

RECOMMENDATION NUMBER 1.s.: We recommend that the Defense Logistics Agency contracting officer require the William Langer Jewel Bearing Plant to provide for a reasonable allocation of general and administrative expenses to jewel bearing and dosimeter operations. (Page 8).

DLA COMMENTS: Concur with recommendations 1.s. DLA will review accounting procedures for allocating costs and expenses to dosimeter operations and provide any instructions and revised procedures considered necessary.

Concur with the internal control weakness cited; however, the weakness is not considered material.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 June 90
() Action is considered complete.

MONETARY BENEFITS: None.

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T. McCoy for Richard J. Connelly

ENCLOSURE 2

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TYPE OF REPORT: AUDIT

DATE OF POSITION: 22 Feb 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: William Langer Jewel Bearing Plant (Project No. 9SS-0049

RECOMMENDATION NUMBER 2: We recommend that the Defense Logistics Agency contracting officer disallow \$1,084 as unreasonable costs related to optical safety. (page 6).

DLA COMMENTS: Concur with recommendation 2. Cost recovery action will be taken.

Nonconcur that an internal control weakness exists. The internal control is the contract requirement to perform a periodic audit to reconcile costs. Since the audit identified unreasonable costs during the reconciliation, we feel the internal control is in place and working.

DISPOSITION:

- (X) Action is ongoing; Final Estimated Completion Date: 30 Jun 90
() Action is considered complete.

MONETARY BENEFITS: To be determined

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: J. T. Consiglio, DLA-NC, 535-7124

DLA APPROVAL: Helen T McCoy for Richard J. Connally

AUDIT TEAM MEMBERS

**Donald E. Reed, Director, Logistics Support Directorate
James Helfrich, Program Director
John Gregor, Project Manager
Ted Paulson, Auditor
Michael Starr, Auditor**

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